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C O N F I D E N T I A L SECTION 01 OF 02 ASHGABAT 001466

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E.O. 12958: DECL: 11/03/2018
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SUBJECT: TURKMENISTAN POSSIBLY AFFECTED BY RUSSIAN
FINANCIAL PROBLEMS

Classified By: Charge d'Affaires a.i. Sylvia Reed Curran for reasons 1.
4 (B) and (D).

11. (SBU) SUMMARY: According to a local expat source, Turkmenistan is feeling the effects of Russia's economic problems. Most significant would be decreased revenue from Turkmenistan's gas exports. Turkmenistan has also seriously overcommitted itself on future gas exports, including to Russia and China, and must undertake additional gas extraction projects if it is to fulfill these commitments. A fall in natural gas prices might force the Turkmen government to rethink some of its spending choices, for example high profile construction projects, and to budget more carefully. END SUMMARY.

TURKMEN FEELING THE PINCH OF REDUCED GAS REVENUES

12. (C) According to longtime Turkmenistan resident and EU-Tacis Advisor Michael Wilson (please protect throughout), Turkmenistan is feeling a revenue crunch because of Russia's current economic crisis. Currently, Turkmenistan relies almost entirely on Russia for state revenue, based on proceeds from its gas exports. Wilson said his contacts in the Turkmen Embassy in Moscow told him that the Turkmenistan MFA tasked them to follow up with Gazprom on gas payments that have been late for the past two months. (NOTE: Because yet another payment just became due at the end of October, it is too early to say whether this pattern of late payment will become habitual. END NOTE.) The higher gas prices paid to Turkmenistan in 2008 put a squeeze on Gazprom, lowering its profit margin. According to Wilson, a 20-percent increase of transit fees will soon be passed on to the consumer.

GAS CONTRACT PRICES TO TREND DOWN IN THE FUTURE

13. (C) Wilson pointed out that Turkmenistan cannot expect to negotiate the same prices that it currently receives in upcoming gas contracts with foreign buyers. He mentioned in particular a new contract with Iran that should be signed by the end of 2008. Turkmenistan expects prices to reach \$400

per thousand cubic meters (tcm). Iran expects to pay \$280 per tcm. Wilson believes the final price probably will end up somewhere close to the lower. Wilson added that falling worldwide oil prices will affect gas contract negotiations with Kazakhstan and Uzbekistan as well.

MORE OPPORTUNITY FOR WESTERN MAJORS?

14. (C) Wilson believes that Gazprom's straitened financial circumstances, and a corresponding decrease in its ability to provide concessional financing for exploration and production activities in Turkmenistan, will improve the chances of major international oil and gas companies that are angling for onshore agreements. Wilson pointed out that Turkmenistan's many gas delivery commitments make it imperative for the country to gear up -- immediately -- if it is going to fulfill them, as it takes a minimum of four years for new projects to come online.

OPTIONS TO SATISFY GAS COMMITMENTS

15. (C) In Wilson's view, Turkmenistan has three options for further development of its gas sector:

-- Allow Western majors to work onshore.

-- Extract gas from an additional 27 fields located in Ahal province that a second Gaffney Cline audit should reveal sometime in the January-March 2009 timeframe.

ASHGABAT 00001466 002 OF 002

-- Work with Russia and China to sink ten or 20 new wells in currently known fields. These would be wells that TurkmenGas has the ability to self-finance. Of the three options, Wilson feels that Turkmenistan is most likely to pursue this approach. However, since this additional drilling would seriously deplete those reserves, Turkmenistan would nevertheless need to commence additional projects immediately.

16. (C) Work on all three of these directions would generate 150 billion cubic meters per year by 2015. Currently, Turkmenistan is only producing about 70 billion cubic meters per year -- at the very most, 80 billion cubic meters.

BACKGROUND ON THE GAFFNEY CLINE AUDIT

17. (C) Wilson said that Gaffney Cline officials were not allowed to inform President Berdimuhamedov that extraction of the deadly high-sulfur gas prevalent in the country will require the assistance of Western majors, because this was considered "bad news." Deputy Chairman for Oil and Gas Tachberdi Tagiyev will "try all options" before informing Berdimuhamedov about these particular Gaffney Cline findings. Wilson heard that the Chinese have lost approximately 40 people due to exposure to sulfurous gas, and Gaffney Cline confirmed that several people were killed as well.

18. (C) COMMENT: While Turkmenistan has isolated itself quite successfully from international financial markets and hence fallout from the current economic crisis is negligible, it relies heavily on revenue from gas sales to Russia. A fall in gas prices may force Turkmenistan to rethink some of its spending choices, for example grandiose construction projects (septel), and to budget more carefully. While the Turkmen government continues to deny Western majors access to onshore production projects, the day may not be too far off when it realizes it has no choice other than to welcome them as partners. END COMMENT.
CURRAN